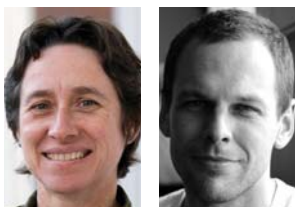


# BUDGET

CHANGE

## How new laws balance budgetary powers



BY CHRISTINA MURRAY  
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Constitution has safeguards that ensure the Executive can no longer unilaterally dictate fiscal policy and the Legislature cannot do as it wishes without upsetting economic and political stability

The 2010 Constitution has made dramatic changes to the Budget process. These open it up to a wider set of actors, particularly giving citizens and MPs a greater role, and fundamentally reducing the traditional, undemocratic and nearly unlimited powers of the Executive. Yet, radical changes in the Budget process can lead to confusion about roles. This must not become an excuse for poor financial management. To ensure continued financial stability and sustainable expenditure, a collaborative relationship between the Treasury and Parliament is needed.

This article spells out the way the Constitution governs the process of adopting the annual national Budget; raises questions about areas where the process may create uncertainty or instability; and suggests some mechanisms to foster a co-operative and prudent approach.

### The new budgetary balance of power

Under the old Constitution, what are referred to as “Money Bills” — such as the Appropriation Bills that authorise spending and Bills introducing taxes — could

be introduced only “upon the recommendation of the President”. Moreover, even most amendments to such Bills required presidential consent. This helped to ensure that the President had firm control of financial matters in Kenya.

If Parliament wished to change a Budget proposal, to allocate more money to one programme or department and less to another, it required the approval of the President. Parliament’s only leverage was to reduce an existing item, or to refuse to pass the Budget altogether, bringing government to a standstill — and jeopardising its members’ own salaries.

The 2010 Constitution is very different. It does prescribe a special process for Money Bills but now much power lies with a parliamentary committee and the

#### KEEPING FOCUS

**If Parliament attempts to act unilaterally, it risks damaging the economy. The most sensible option is to enable institutional processes that safeguard against the potential risks of having a Parliament with strong budgetary authority**

National Assembly, not the Executive. To work effectively the new process requires careful coordination and consultation between the Executive and the National Assembly:

#### 1. The budget process will have two components:

Because all revenue raised by the national government must be shared with the counties, the first step is for the annual Division of Revenue Bill to divide revenue raised nationally between the national government and the county level of government (Article 218).

The Division of Revenue Bill is not a “Money Bill” (Article 114(3)). Accordingly, it goes through Parliament in the ordinary way and must be passed by both the National Assembly and the Senate (Articles 110 and 112).

Second, the revenue allocated to the national level of government must be dealt with through a process involving the introduction of Budget estimates (that is, proposals as to how the money should be spent) and then the annual Appropriation Bill (which authorises the Executive to spend).



Unlike Finance Minister Uhuru Kenyatta, who is an MP, the Cabinet Secretary for Finance will be picked from outside the Legislature.

Counties will adopt their own budgets based on the revenue they raise themselves as well as their share of the revenue raised nationally, that is divided among the counties in a special County Allocation of Revenue Act.

**2. Three separate sets of “Budget estimates” will be submitted to the National Assembly:**

These are those for the expenditure of the national government prepared by the national Treasury (Article 221(1)); those for the parliamentary service (Article 127(6)); and those for the Judiciary (Article 173(3)).

In a departure from the position under the old Constitution and section 12 of the Financial Management Act, 5 of 2008, the Constitution does not require estimates for the parliamentary service or the Judiciary to be considered by the national Treasury before they are submitted to Parliament. Of course, it would be wise and more efficient to have a process in which the separate Budget proposals are considered together in advance so that what is put to the National Assembly is realistic. We discuss this further below.

**3. The Cabinet Secretary responsible for Finance cannot formally introduce either government Budget estimates or the Appropriation Bill in the National Assembly because he or she (previously known as the Minister of Finance) will not be an MP (Article 152(3)).** Only MPs or parliamentary committees may do this. Instead, it is likely that the Cabinet Secretary will send these to the Speaker or a committee of the National Assembly. Then, presumably, they will be handled according to new Standing Orders.

**4. The three sets of Budget estimates will be considered by a potentially very powerful committee of the National Assembly which will exercise considerable control over the budget process.** That committee must “discuss and review the estimates and make recommendations to the Assembly” (Article 221(4)).

In the process, the Committee must “seek representations from the public” and take those representations as well as the views of the Cabinet Secretary for Finance into account. Although the Constitution says that the committee makes “recommendations” to the Assembly, in fact, the Assembly cannot amend the estimates the committee adopts.

Article 114(2) says that, if the Assembly is asked to make a decision on anything listed in the definition of a Money Bill, “the Assembly may proceed only in accordance with the recommendation of the ... Committee after taking into account the views of the Cabinet Secretary responsible for finance”. So, the Committee must table its recommendations concerning the estimates together with the views of the Cabinet Secretary in the House but the Assembly has only two courses of action open to it: to accept the committee’s recommendations or to reject the estimates entirely. The

amendment process takes place in the committee.

**5. An Appropriation Bill is introduced once the National Assembly has approved the estimates. It must reflect the National Assembly’s decisions on the estimates.**

The most radical change in this new process is the power it gives the National Assembly, through the Article 221(4) committee, to amend the Budget.

In the September 2011 edition of *The Nairobi Law Monthly*, Mr Mohamed Wehliye suggested that the National Assembly does not have this power because the Constitution does not expressly grant the power to amend Money Bills to the Assembly (*Pitfalls of Parliament’s Power over Public Purse*). But this misunderstands the Constitution. First, Mr Wehliye does not give due weight to the statement in Article 114(2) of the Constitution that the National Assembly must “take into account” the views of the Cabinet Secretary for Finance. This wording signals a clear departure from Section 48 of the old Constitution. It means that the National Assembly is not bound by the views of the Cabinet Secretary (or President). All that it is obliged to do is to consider those views.

Secondly, because three separate sets of estimates may be submitted directly to the National Assembly, without going through the national Treasury, some opportunity to make adjustments to Budget estimates in Parliament is essential. If the Treasury has had successful interactions with the Parliamentary Service Commission and the Registrar of the Judiciary in advance and has also given the Assembly early warning of what it is intending to present in the Budget estimates, the National Assembly will probably not need to make adjustments.

But, if there has not been early agreement on the three budgets, it is unlikely that added together they will match exactly the money available for appropriation. The National Assembly then needs to be

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able to manage any mismatch and ensure that authorised expenditure is within realistic limits. Thus, without the power to amend Budget estimates, there would be no way of managing the overall Budget.

The power to amend the Budget places a great responsibility on the National Assembly. The Budget and tax Bills are the foundation of the economic health of the country. They need to be managed carefully in order to build a strong economy.

If MPs react too readily to the many short-term needs of their voters, and compromise long-run sustainability, the country will be worse off. The present economic environment, in which a current account deficit, inflationary pressures and a depreciating currency are combined, is not an easy one in which to respond to the expectations of ordinary Kenyans. This in turn means that the Article 221(4) committee will need considerable expertise and wisdom to understand what spending is essential and to manage the process properly. It also means that there must be ongoing consultation between the Executive and the National Assembly in settling the Budget.

Of course, although the emphasis here has been on the new role of the National Assembly, the Executive does not lose all its influence in the process once the Cabinet Secretary submits the government's estimates to the National Assembly. The President may refuse to sign the Appropriation Bill approved by the National Assembly. Under such circumstances, the Bill will be referred back to the National Assembly and the Assembly will have either to accommodate the President's reservations or pass it by a two-thirds majority, failing which it is back to the drawing board.

The Constitution does provide a safety net for the Executive in such circumstances. As in the previous Constitution (Article 101), Article 222 of the 2010 Constitution allows the National Assembly to authorise spending prior to the approval of the Budget. Such "vote on account"

provisions exist in many Commonwealth countries.

When partisan control of the legislative and Executive branches is divided, however, parliamentary approval of interim spending can no longer be taken for granted. The political and economic consequences of a failure to adopt a Budget and the resulting government "shutdown" are potentially highly damaging. To avoid this, the National Assembly must take the views of the Executive very seriously. The President's power to veto the Appropriation Bill should influence the way in which the Standing Committee and National Assembly deal with the estimates and the Bill. It is in no-one's interests to have the Budget blocked by a standoff between the Executive and the Legislature.

There may be subtler and less overtly confrontational ways in which the Executive shapes expenditure. For instance, strategic underspending may allow the President to limit outlays on items in the approved budget that the Executive considers excessive. This is a common tactic in presidential systems with legislatures that play a visible role in Budget approval, such as Brazil and Nigeria. Over time, such non-disbursement of approved funds, or "impoundment", may also lead to heightened conflict and mistrust between the branches.

As we note at the outset, to avoid stand-offs and other conflicts the relationship between the Executive and Legislature needs to be properly managed. Many countries have established processes by which the Budget is discussed between MPs and the Executive long before it is

introduced in the Legislature. We discuss this later. Before moving there, however, attention must be paid to the provisions of the draft Public Finance Management Bill (PFMB – all references refer to the harmonised draft dated November 24, 2011, retrieved from [www.treasury.go.ke](http://www.treasury.go.ke)).

A law cannot limit Parliament's power to amend Money Bills

It is evident that the drafters of the PFMB were alert to the potential challenges of a new balance of power associated with a system in which the legislature has unlimited authority to amend money bills, because the draft Bill seeks to place firm limits on the power of the National Assembly. It does this first by requiring the National Treasury to prepare a Budget Policy Statement each year and submit it to Parliament (clauses 25 and 37 of the draft PFMB).

Parliament is given 14 days to adopt a report on the Budget Policy Statement and the Cabinet Secretary for Finance must take this report into account in finalising the Budget. However, in terms of the draft Bill, he or she is neither obliged to follow recommendations in the report in finalising the Budget nor required to amend the Budget Policy Statement to comply with them. Later the PFMB refers to a Budget Policy Statement that has been "adopted" by Parliament. This may point to a drafting error and suggests that the drafters of the PFMB intended to require Parliament to adopt the Budget Policy Statement. If so, Parliament's amendment powers would have been protected to some extent although the two-week time frame is short. Secondly, the PFMB limits the ways in which the National Assembly may amend the Budget estimates and the Appropriation Bill. On the estimates it states in clause 39(3):

"The National Assembly can amend the budget estimates of the National Government only in accordance with the policies set out in the Budget Policy Statement adopted by Parliament and only if—

#### DIFFERENT STROKES

**The parallels between the South African and Kenyan constitutions do not apply in the case of the amendment of Money Bills because the wording of the two constitutions and the Budget processes they envisage are different**

- (a) any increase in expenditure in a proposed appropriation is balanced by a reduction in expenditure in another proposed appropriation; or
- (b) any proposed reduction in expenditures is used to reduce the deficit.”

Clause 39(4) deals with the adoption of any Money Bill which includes the annual Appropriation Bill:

“The National Assembly shall consider all money Bills in accordance with Article 114 of the Constitution, and only if—

- (a) any increase in expenditure in a proposed appropriation is balanced by a reduction in expenditure in another proposed appropriation; or
- (b) any proposed reduction in expenditures is used to reduce the deficit.”

Thus, under the PFMB, when dealing with Budget estimates Parliament would be bound both by the Budget Policy Statement prepared by the Treasury and by paragraphs (a) or (b) of clause 39(3). The PFMB is less clear on what it proposes for Money Bills such as the Appropriation Bill as there seems to be an omission in the introductory words to clause 39(4).

Taking a lead from 39(3) one can speculate that what was intended was “The National Assembly shall consider all money Bills in accordance with Article 114 of the Constitution, and can amend the money Bills only in accordance with the policies set out in the Budget Policy Statement adopted by Parliament and only if...”

Although the explicit reference to Article 114 here is puzzling (Article 114 applies to Motions involving public finances and not only Bills and thus is equally relevant to the Budget estimates), the inclusion of paragraphs (a) and (b) in clause 39(4) make it clear that the PFMB intends to bind Parliament.

Mr Wehliye argues that the provisions of the draft PFMB that purport to give Parliament the power to amend the Budget are unconstitutional because, as he reads it, the Constitution does not give Parliament

that amendment power and so Parliament cannot assume that power by passing a law. Our concern is completely different: we agree that the proposals in the draft PFMB are unconstitutional but we would argue that they are unconstitutional because they limit the constitutional power of Parliament to amend the Budget.

We have explained above how the 2010 Constitution gives Parliament the power to amend Money Bills. But, why, it might be asked, can Parliament not restrain itself by passing a law like the PFMB? The answer is because the Constitution establishes a balance of power between the Executive and the Legislature which Parliament cannot disturb. The “checks and balances”, to use American terminology, on the exercise of power in the new constitutional arrangements are most obvious when it comes to appointments to senior positions.

For instance, the President nominates his or her Cabinet members but may appoint them only with National Assembly approval (Article 152(2)). Thus, the Legislature exercises a check on the Executive. The “power of the purse” is another significant check. By giving the National Assembly real control over the Budget through the power to adjust the estimates, subject always to presidential veto, the Constitution ensures that the Executive’s power to spend is constrained.

If a law were to be passed limiting this parliamentary check on Executive power, the National Assembly would have removed an important check on power and subjected itself to the Executive: just as the assent of the President is required for the Bill to become law, so his or her assent would be needed to repeal it.

Accordingly, in effect, the proposed Act would hand a power that the Constitution allocates to Parliament to the Executive and lock not only the current National Assembly but also future Assemblies into a system of Budget review that bolsters Executive power at the cost of the power of the Legislature.

Mr Wehliye correctly reminds us that the South African Constitution was an influential source for the provisions on Public Finance in the Kenyan Constitution, but here the South African model is not useful. Contrary to Mr Wehliye’s suggestion, Kenya does not need to follow the South African process to give Parliament the power to amend Money Bills. First, the parallels between the South African and Kenyan constitutions do not apply in the case of the amendment of Money Bills because the wording of the two constitutions and the Budget processes they envisage are different.

Secondly, Mr Wehliye is wrong in saying that the South African Constitution was specially amended to allow amendments to Money Bills. In fact, when it was enacted in 1996, Section 77(2) of the South African Constitution stipulated that: “An Act of Parliament must provide for a procedure to amend money Bills before Parliament”. This provision became Section 77(3) when an additional subsection was added to Section 77 but its wording remained unchanged.

In the South African context, Section 77(3) is a response to South Africa’s particular history in relation to Money Bills. It serves two purposes: (i) It makes Parliament’s power to amend Money Bills explicit (as do Articles 114 and 221 in the Kenyan Constitution); and (ii) it ensures that the power of the South African Parliament to amend Money Bills cannot be nullified by the (easy) amendment of standing orders by the (strong) majority party as was the case in the past. In other words, it was the intention of South Africa’s constitutional drafters from the outset to manage a process by which amendments to Money Bills could be introduced through an Act of Parliament.

It appears that the drafters of the PFMB laboured under the same misapprehension as Mr Wehliye about the similarity between the South African and Kenyan constitutions. In many ways the provisions of the PFMB mirror those of the South

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African Money Bills Amendment Procedure and Related Matters Act 9 of 2009. Among other things, that Act regulates the Budget process in South Africa's Parliament. It requires the South African national Treasury annually to table in Parliament a fiscal framework (similar to the Budget Policy Statement of the PFMB) and requires amendments to Money Bills to be consistent with that framework.

But, it gives the South African Parliament more influence over the budget process than the Kenyan PFMB gives the Kenyan Parliament. The South African Act clearly allows MPs to amend the proposed fiscal framework. Moreover, in theory at least, it is easier for South African MPs to repeal their Money Bills Amendment Procedure Act than it would be for Kenya MPs to repeal the PFMB once adopted because, as is customary in parliamentary systems like the South African one, the South African President may not refuse to sign a Bill into law unless he or she believes it to be unconstitutional.

By contrast, as noted above, the Kenyan President, as head of the Executive in a presidential system may veto any Bill and Parliament can override this veto only if it secures the support of two thirds of the members of the National Assembly and two thirds of the delegates to the Senate.

## Avoiding fiscal stalemate

Kenya is not the only country to grant extensive budgetary powers to its Legislature. Among the 34 member countries of the Organisation for Economic Co-operation and Development (OECD) — a grouping of the world's industrialised democracies — about half have national legislatures with unfettered constitutional authority to amend the Budget. The UK model — from which the provisions on Money Bills in Kenya's previous Constitution were copied — is an outlier among the OECD countries, due to the severity with which it restricts parliamentary participation in fiscal decisions. Moreover, legislative amendment authority in bud-

etary matters is not a luxury reserved for rich nations. A 2008 survey of budget systems in 26 African countries, conducted by the Collaborative Africa Budget Reform Initiative (CABRI) and the African Development Bank, found that many had legislatures with extensive budgetary powers: five were categorised as having unlimited amendment authority, and a further seven were classified as allowing substantial changes — such as reallocations between programmes or ministries — as long as the total deficit or total spending remained unaltered. Among the countries with severe restrictions were mostly former British colonies that simply copied the UK's restrictions into their post-colonial constitutions, such as Zambia and Zimbabwe.

Economists in particular tend to worry that legislative bodies with strong authority may be fiscally dangerous. One argument highlights the so-called “common-pool-resource problem” in budgeting. This theory suggests that legislators have a tendency to vote spending that benefits their constituency while the costs are distributed more widely. In the jargon of economics, legislators may fail to “internalise” the full cost of their actions, giving rise to “fiscal illusion” and excessive spending.

Another argument is that legislative involvement may delay government in situations when quick fiscal action may be desirable, for instance in response to an economic shock. There is empirical evidence that such concerns are valid if these tendencies go unchecked. These theories have often been used to argue in favour of Budget processes that are dominated by strong Finance ministers, who can over-

### FISCAL ILLUSION

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rule both Cabinet colleagues as well as parliamentarians. However, many countries with strong legislative bodies have found mechanisms that can help to mitigate these risks.

One mechanism is for the Finance ministry (or the Treasury) to collaborate with Parliament prior to the tabling of the annual Budget. In some countries, this takes the form of a “top-down” process in which aggregate totals are fixed before making choices about individual programmes or items in the Budget.

In Sweden, five months prior to the Budget, the government tables a Spring Fiscal Policy Bill that contains broad guidelines. This means that legislators have a chance to debate and formally shape and approve the direction of fiscal policy several months before the budget for the upcoming year is tabled. Once the Budget is tabled, parliamentarians approve the totals before they vote on individual spending areas. A similar process is followed in Indonesia, a presidential system, where the government uses a pre-Budget report as an opportunity for committee discussions of fiscal policy and Budget priorities, including allocations to ministries. This report is tabled three months prior to the annual Budget and more than seven months ahead of the relevant fiscal year. Other countries require governments to produce formal pre-Budget reports, such as South Africa's Medium-Term Budget Policy Statement.

In Kenya, the Budget Policy Statement could serve to build early consensus with MPs and give the Treasury a sense of what they expect to see in the annual budget. However, the Budget Policy Statement is currently published little more than three months prior to the beginning of the fiscal year — several months later than in the countries discussed above. The current draft of the PFMB (clause 25(2)) requires publication by the end of February. This is a step in the right direction, although we would advocate a deadline in January.

Timely debate of the Budget Policy

Statement in the National Assembly would help to ensure that potential conflicts are resolved early, rather than stored up until the discussion of the annual Budget. It should also be used to clarify the division of revenue between the national government and counties, as well as allocation across the counties, so that budgets can be drafted that reflect this division. The draft PFMB (clause 186) envisages precisely such a process.

A second mechanism that can help to contain the “common-pool-resource problem” is to ensure that budgetary decisions in the Legislature are centralised in a powerful financial committee. In the United States, this was the intention when the Budget committees were created as part of wide-ranging reforms in the 1970s. Previously, a number of different committees had jurisdiction over spending decisions, without overall co-ordination to ensure cohesive fiscal policy decisions.

One of the reasons why the US struggles at present to formulate a coherent plan for fiscal consolidation is that the Budget committee process has broken down, so that Congress no longer has an effective co-ordinating mechanism for reconciling available totals with particularistic choices about individual programmes.

When Sweden overhauled the parliamentary process in the mid-1990s, it also greatly strengthened the role of the Finance Committee vis-à-vis sectoral committees, which previously dominated the process. Similarly, South Africa’s new parliamentary Budget process relies on the finance and appropriations committees to co-ordinate amendment proposals.

Articles 114(2) and 221(4) of Kenya’s Constitution provide the basis for a powerful committee to arbitrate demands on the Budget. If effectively implemented, this should ensure that the Budget process in the National Assembly does not deteriorate into an unsustainable free-for-all.

Internationally, the most influential Budget committees are composed of members with relevant professional

backgrounds and academic qualifications, such as degrees in economics or accounting, and who can acquire expertise in public finance by spending a number of years on the committee. Given the central importance of this committee, it will be essential to ensure that appointments to Kenya’s Budget Committee strike a careful balance between political clout and economic expertise.

In addition, a range of other institutional features can help support constructive engagement by the Legislature. Notably, a properly staffed legislative Budget Office can provide objective, non-partisan analysis on budgetary issues. A growing number of countries has established or are in the process of establishing such offices, including Uganda and, more recently, South Africa. Kenya’s Parliamentary Budget Office, established by the 2009 Fiscal Management Act, is still young. It needs to be carefully nurtured to play a credible supporting role, by providing high-quality and independent technical analyses. The Budget Office needs capacity to assess Executive Budget proposals, monitor execution, cost the impact of proposed and approved parliamentary amendments, and investigate medium-term patterns. The systematic costing of individual pieces of legislation, as envisaged in Clause 9 of the draft PFMB, would require a significant expansion of sector-specific expertise (health, education, agriculture, etc).

In addition, the Budget should be tabled well in advance of the start of the fiscal year so that Parliament can exercise its constitutional responsibility. It is generally accepted that thorough scrutiny of the Budget requires a minimum of three months, although some Legislatures have more time – for instance, eight months in the United States, and five in Germany. Clause 37(2)(b) of the draft PFMB would require the Budget to be tabled by April 30, as required by the Constitution (Article 221(1)). Again, this calls upon the Treasury to rethink its established processes, so that it can deliver the Budget on

time and in line with the Constitution. Ideally, the annual Budget should be tabled in late March, preceded in January by the publication of the Budget Policy Statement and the Division of Revenue and County Allocation of Revenue Bills.

To sum up: The 2010 Constitution provides for a new balance of budgetary power, where the Executive can no longer unilaterally dictate fiscal policy. This fact cannot be undone by imposing new limits on parliamentary authority in public finance legislation. Moreover, if the Executive responds by simply trying to maintain its old habits from times when it could unilaterally dictate the Budget, it will end up stoking political tensions rather than managing them.

Similarly, if Parliament attempts to act unilaterally, it risks damaging the economy. The most sensible option is to enable institutional processes that safeguard against the potential risks of having a Parliament with strong budgetary authority. We highlighted several such mechanisms, in particular an effective pre-budget debate that establishes a clear fiscal framework early in the drafting process, and a powerful Budget Committee in the legislature. Sound analytic support for MPs and a well-timed parliamentary budget process are also important. Clearly, political factors will determine a great deal of what the new constitutional provisions will mean in practice. Institutional engineering may have its limits, but if carefully done it offers the best bet for reconciling the new budgetary balance of power with a sustainable fiscal future. ■

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